Supreme Court of the United States

OCTOBER TERM, 1947

Nos. 184-9

IN THE MATTER

of

THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY, COMPANY,
Debtor.

THE CHICAGO, ROCK ISLAND & PACIFIC RAILWAY, COMPANY,
Debtor-Petitioner,

v.

METROPOLITAN LIFE INSURANCE COMPANY, as remaining member of the First and Refunding Group, CENTRAL HANOVER BANK AND TRUST COMPANY, *et al.*, as Trustees, THE NATIONAL CITY BANK OF NEW YORK, as Trustee, J. HAMILTON CHESTON, *et al.*, JOHN C. TRAPHAGEN, *et al.*, JAMES G. BLAINE, *et al.*,

Respondents.

REPLY BRIEF OF DEBTOR-PETITIONER

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New York, New York, September 11, 1947.

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CITATIONS

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The debtor believes it necessary to reply briefly to some of the assertions and arguments in Respondents' Brief.

1. *Applicability of the Denver opinion of this Court,* 328 U. S. 495.

Events occurring since the filing of debtor's petition herein bring into sharper focus the fact that the question before this Court is:

May the District Court, or the District Court and Commission* acting together, reconsider the fairness of a plan when the following facts appear: (1) the plan had previously been approved by the Court and Commission; (2) the plan had thereafter been rejected by adverse votes in excess of 75% by two important classes of creditors; and (3) the District Court has found that the rejections were reasonably justified by a large and unanticipated increase in the earnings of the debtor *after the plan had been approved?*

The Circuit Court of Appeals held, and respondents contend, that increased earnings after approval of the plan, no matter how great, must be conclusively considered as having been anticipated by the Court and Commission when they approved the plan (even though the Court later asserts that it did not anticipate such earnings, and the Commission is prevented from stating its views). This Court's *Denver* decision, 328 U. S. 495, is relied upon as establishing this principle.

Petitioner contends that in the *Denver* case no argument was made that facts occurring *after* approval of the plan required its consideration but reliance for reconsideration was placed entirely upon facts which occurred *prior* to approval of the plan, as to which this Court held the order of approval was *res judicata.* In that case the power of the District Court to direct a reconsideration of the plan, after approval, because of subsequent unanticipated earnings, was expressly recognized (328 U. S. 495, 535):

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* In this case the Commission did not express its views as to the desirability of reconsideration of the plan. It held that it was powerless to do so while the appellate courts were in process of reviewing the order of the District Court refusing confirmation of the plan and referring it to the Commission for further consideration. In practical effect, therefore, action such as that followed by these respondents effectively blocks a reconsideration of the plan even when both Court and Commission deem such action desirable in the light of changed conditions.

"Reasons to make [creditors'] rejection reasonable may arise [after approval]. For example, unanticipated, large earnings might develop."

2. *The debtor's earnings throughout the post war period demonstrate a consistent earning power of more than double the Commission's estimate: this is the prime type of unforeseen circumstance of which this Court spoke in the first Denver case,* 328 U. S. 495, 535.

The so-called "normal" earnings of the Rock Island which would be available for the payment of interest on indebtedness were predicted by the Commission to be $11,000,000 (242 I. C. C. 298, 437). On this prediction the rejected plan was based. Yet the debtor's earnings have consistently been *more than twice* this figure.

Analyses of the earnings data available when the debtor's petition for certiorari was filed are stated therein (pp. 21-6, 29-31). The Trustees' figures for the first seven months of 1947 are now available:

EARNINGS OF ROCK ISLAND
January 1-July 31, 1947

Earnings (after deduction of depreciation, amortization, and federal income taxes, and before deduction of interest, accrued but unpaid on all outstanding bonds)	$12,008,706.
Federal income taxes (added to earnings because taxes are deducted after bond interest has been paid)	2,968,000.
Total earnings available for interest on old bonds	$14,976,706.
Interest on all old bonds	7,166,273.
Excess of earnings during the first seven months of 1947 over interest requirements on all the old bonds	$ 7,810,433.

Interest on all the old convertible bonds was earned more than ten times during this period,* as shown by the following figures:

Total earnings available for interest on all outstanding bonds (from foregoing table)	$14,976,706.
Interest on outstanding bonds which are senior to the convertibles	6,318,900.
Earnings available for interest on convertibles	$ 8,657,806.
Interest accruing on the convertibles	$ 847,350.

These figures—of earnings during one of the worst periods in the history of our railroads—are of vital importance to all who have invested in the Rock Island; they show that the I. C. C. was grossly mistaken in its prediction of earnings for the railroad; they put meaning into the overwhelming rejection by two creditor classes of the reorganization plan; they justify Judge IGOE's refusal of confirmation and remission of the plan to the Commission for a reexamination, not necessarily a change, of its work.

Respondents in their brief assert as a main thesis that no unexpected change or condition exists within the meaning of the first *Denver* case, 328 U. S. 495, 535. If continuous earnings of more than twice the estimate of I. C. C. are not an unanticipateed circumstance making a plan's rejection reasonable, what is?

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* The holders of which are paid only 17% of their claims for principal and interest under the plan. They rejected the plan by an adverse vote of over 75%.

3. *The attitude of the Congress and of the Interstate Commerce Commission is that pending railroad reorganization plans are unfair, and under Section 77 unfairness can be removed.*

Throughout respondents' brief the opinion of the District Court (R. 249-53) refusing confirmation of the rejected plan is belittled for referring to the unrest of Congress and the I. C. C. with respect to present "forfeiture plans" under Section 77 and the possibility of a new reorganization law. The purpose of Judge IGOE's reference was not speculatively to look to possible legislation and to decide the *Rock Island* case by what the law might be in the future. Instead, he quoted Congressmen and the Commissioners to show the unfairness of the rejected plan under present law—under Section 77—and wholly in accordance with that law he refused confirmation. It is obvious that the courts cannot wait for possible legislative changes in reorganization proceedings any more than in other types of cases. This Judge IGOE did not do nor purport to do. Section 77 and the demonstrable unfairness of the rejected plan governed his decision.

The lack of satisfaction with pending railroad reorganization plans has continued, and increased. The Senate Committee on Interstate and Foreign Commerce and the House Committee on the Judiciary during the first session of the Eightieth Congress both commented on the inequities of the *Rock Island* plan in view of that railroad's unanticipated capacity for earnings. An important statement issued by our Congressional leaders on this subject as recently as August 1, 1947, is fully reproduced in Appendix A to this brief, *infra*, pp. 11-15.

The nature of the new legislation which is proposed is not now important; this case must be decided under Section 77. What is important is that conditions in the *Rock Island* and some of the other reorganizations are suffi-

ciently inequitable to cause the Congress, busy with problems of world importance, to consider reorganization legislation. When railroad reorganizations are criticized by the Congress and public to such an extent, it is patently justifiable to use machinery expressly created by Section 77(e) for exactly this situation:

> "If the judge shall not confirm the plan, he shall * * * in his discretion * * * refer the case back to the Commission for further proceedings."

The outstanding development in this line is that the Interstate Commerce Commission, recognizing the change of economic conditions since approval of the reorgnization plan for the Missouri Pacific system, requested the district court to remit the plan to it for further consideration.** This action in indicating the Commission's attitude toward present plans is so important to the present case that the I. C. C.'s memorandum requesting remand is reproduced in full in Appendix B to this brief, *infra*, pp. 16-23.

In its memorandum brief on remand of the Missouri Pacific plan, the Commission develops two reasons which it states are adequate to justify remitting the plan for reconsideration:

> (1) extensive expenditures made for improvement of the property may affect the earning power of the pany; and

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**It is to be noted that the Commission says (*infra*, p. 17) it has "consistently refrained from volunteering its views on new or changed conditions", believing that any request for its views on reexamination of plans must come from the courts. In the *Missouri Pacific* reorganization the district court approved the plan, and it was not until the circuit court specifically sought the I. C. C.'s attitude that any was expressed. In this *Rock Island* case the Commission, in deference to the appellate court postponed its already scheduled hearings on a reconsideration of the plan and gave no expression to its views.

(2) debt retirement, cash accumulations, and interest payment make adjustments necessary in the distribution of cash and new securities, which "may result in substantial disturbance of the balanced relationship of the treatment provided for the various classes of creditors."

Both these conditions are equally present in the Rock Island reorganization. In addition to these factors is the primarily controlling fact, not mentioned by the Commission in its *Missouri Pacific* brief, that the Rock Island railroad has a well demonstrated earning power which is in excess of twice that predicted by the Commission.

Word has just been received that the Circuit Court of Appeals for the Eighth Circuit has given effect to the Commission's request, and, reversing the order of the District Court, has referred the plan back to the Commission for reconsideration.

4. *The debtor has standing to apply for certiorari, since Section 77 in explicit terms affords that right and every court considering the question has so held.*

Without joining direct issue on the problem, respondents seek indirectly to discredit the debtor's position regarding the main questions in these cases by attacking its status to apply for certiorari (Resp. Brief, pp. 2, 48-50). The same contention was made by respondents before the Circuit Court of Appeals, the District Court, and the Commission, and each time was rejected.

Section 77(c)(13) provides that "the debtor • • • shall have the right to be heard on *all* questions arising in the proceeding." (Emphasis supplied.) Similar language in Section 206 of Chapter X has been held to grant the right to appeal. In re *Keystone Realty Holding Co.*, 117 F. 2d 1003, 1005 (C. C. A. 3d 1941); *Dana* v. *SEC*, 125 F. 2d 542, 543 (C. C. A. 2d 1942).

The debtor makes no contention that it may speak for creditors or stockholders individually. It does contend, however, that it represents the estate as a whole and that its right and duty is to present to the Commission and the courts the respects in which the Rock Island plan of reorganization fails to conform with proper legal and equitable standards. In doing this, the debtor is acting for the benefit of all creditors, secured and unsecured, and all stockholders, preferred and common, who are injured by the fact that the plan is not fair and equitable, except those who act directly in their own behalf, and those who have expressly delegated to committees or other representatives the power to act for them.

Recent cases in this Court clearly recognize the debtor's right to appeal on behalf of the entire estate from approval of a Section 77 reorganization plan even in the face of a finding below that no equity remains in the debtor's property for stockholders. In *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448 (1943) the outstanding stock was found to be valueless by the Commission and District Court, but the debtor was permitted, on a rehearing (p. 140), to appeal to the Circuit Court of Appeals, 124 F. 2d 136, 140 (C. C. A. 9th 1942), was granted certiorari by this Court, 316 U. S. 654 (1942), and argued on the merits of the appeal, 318 U. S. 448 (1943). As shown by the summary of the debtor's argument in that casee (87 L. ed. 907-909), it argued primarily for junior creditors.

In *Group of Institutional Investors* v. *Chicago, Milwaukee, St. Paul, and Pacific R. Co.*, 318 U. S. 523 (1943), the debtor took an appeal from the order approving the plan and was heard in the Circuit Court of Appeals, 124 F. 2d 754 (C. C. A. 7th 1942). Later the debtor briefed and argued as an appellee to this Court, 318 U. S. 523 (1943).

Similarly, in *Reconstruction Finance Corporation* v. *Denver & Rio Grande Western R. Co.*, 328 U. S. 495 (1946),

the debtor, taking appeals from the orders of approval and confirmation, was heard in the Circuit Court of Appeals, 150 F. 2d 28 (C. C. A. 10th 1945), and on certiorari argued the case to the Supreme Court, 328 U. S. 495, 502, 505 (1946). It appears in the opinion of the Court that the Denver & Rio Grande stock had been held valueless, but nevertheless the debtor was permitted without challenge to argue on behalf of creditors.

In the second appearance of the *Denver* case before this Court recognition of the debtor's right to seek review of orders in reorganization was expressly given. Reference was made in the opinion to "the creditors and stockholders whom the debtor represents here * * *." *Insurance Group Committee* v. *Denver & Rio Grande Western Railroad Co.*, 329 U. S. 607, 618 (1947).

All courts dealing with this issue have given recognition to a debtor's right to seek review of the reorganization plan on behalf of creditors as well as stockholders.

A proceeding under Section 77 is not an adversary controversy but an equitable proceeding in which not only the debtor, but the Commission and the courts as well, are charged with the duty of seeing that an equitable distribution of the assets of the debtor is made among its creditors and stockholders. Inequities to classes of creditors, whether secured or unsecured, cannot be tolerated merely because some so-called representative committee has agreed to such inequities. Certainly, no court will ignore inequities in a plan merely because the debtor, rather than a creditors' or stockholders' committee, has called attention to them.

Conclusion

Reorganization proceedings are essentially in equity. Legalisms should be disregarded in favor of the real interests of the parties.

The senior creditors are fully protected by the absolute priority rule. Mortgages must be fully satisfied to the extent of mortgaged assets before general creditors may participate in any excess, and all creditors share equally in unmortgaged assets. Since senior creditors possess this priority which must, in any event, be recognized, it is not unfair to request a reexamination of the plan before millions of dollars in junior investments are destroyed.

All that the debtor seeks is that the Commission be allowed to "check its figures" according to the procedure prescribed in Section 77 before the rejected plan is consummated.

The prayer of the debtor is respectfully renewed that its petition for writ of certiorari in this equitable cause be granted.

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Appendix A

Statement on Pending Railroad Reorganization Legislation.

In view of the widespread interest, both in Congress and throughout the country, in pending legislation to prevent further unnecessary and unwarranted forfeiture or impairment of over two billion dollars par value of investments in railroads now in recognition, a statement of the present status of this legislation appears timely.

That such legislation was not enacted into law during the session of Congress just ended is regretable. That it failed of enactment during the recent session was due partly to the time required for its careful preparation before it was introduced. Similar legislation (S. 1253) was passed in the second session of the 79th Congress by a vote of 2½ to 1 in the House and without a dissenting vote in the Senate. While that measure was pocket-vetoed by the President, his Memorandum of Disapproval clearly disclosed that he favored the objectives sought and approved the broad principles upon which that measure was based. He expressed his belief that the 80th Congress could pass an improved billl which would meet his stated objections and more effectively accomplish its purposes.

In a joint statement issued April 28th of this year, we said:

> "On February 3, 1947, Senator Reed, acting for Senator Myers of Pennsylvania, and Representatives Hobbs and Reed had a most agreeable conference with President Truman. It was agreed that the President would instruct his assistants to confer with the Members of Congress and lend any aid they desired in preparing new legislation which would meet the objections that the President had directed at the previous bill. The bill introduced today by Representative Reed (of

Illinois) (H. R. 3237) is the result of several months intensive study by the proponents on both Houses of Congress and their assistants and of the legislative assistants of the President. Senators Reed and Myers will offer amendments to Senate Bill 249 which will revise that bill in a manner to make it substantially identical with the bill introduced by Representative Reed of Illinois."

The objections of the President to S. 1253 were appropriately met in the new bill (H. R. 3237) introduced April 28th.

That measure was promptly set down for hearing before the Subcommittee on Bankruptcy and Reorganization of the Committee on the Judiciary, and extensive hearings were held on May 12, 13, 14, 15, 16 and 19. (The printed record of such hearings comprises 307 pages.)

On May 8th Senators Reed and Myers issued a Subcommittee print of their proposed amendments to S. 249 which would make that bill substantiallly the same as H. R. 3237. Hearings on S. 249 and those amendments were commenced on the very day hearings on H. R. 3237 were concluded (May 19th), and continued on May 21, 23, 27, 28 and 29, and June 4, 5 and 6. (The printed record of those hearings comprises 596 pages.)

On June 25th, the Subcommittee of the House Committee on the Judiciary, favorably reported a "clean bill" (H. R. 3980).

On July 3rd the Senate Committee on Interstate and Foreign Commerce favorably reported S. 249 with amendments that made that bill substantially identical with H. R. 3980.

On July 15th, after considering H. R. 3980 at several executive sessions, the Committee on the Judiciary reported

the bill favorably. An application for a rule was then made to the Rules Committee. Hearings thereon were held by that Committee on July 18th and 21st. On the latter date (but five days prior to the scheduled adjournment of the session) the Rules Committee voted not to grant a rule at that session. A reconsideration of this vote on July 25th was blocked on a point of order, on the ground that the Committee had theretofore agreed not to vote out a rule at that session.

As with many other bills before Congress in the recent session, the pressure of pending appropriation bills and other urgent legislation made it impossiblee to obtain a vote on these railroad measures during the closing days of the session. That this legislation will be promptly considered when Congress reconvenes is regarded as certain.

Particularly in view of the fact that Governmental agencies themselves are largely responsible for the drastic character of pending reorganizations, which led to extensive litigation and delay, we are confident that the Congress will favorably consider these remedial measures. They are intended to remedy policies initially put into effect by one of Congress' own agencies, the Interstate Commerce Commission. In general, the courts have declined to give full judicial review to the plans and policies of the Commission, stating that only Congress can so direct or otherwise grant relief. We believe Congress will act again upon this suggestion, as it did last year in the passage of S. 1253.

While the desirability of concluding pending reorganizations and returning the properties to private management is fully recognized, it is of vastly greater public importance that justice be done and that investments in our railroads be not needlessly destroyed or seriously impaired merely for haste.

In fact, haste at this juncture will cause a great deal indeed to be uselessly sacrificed. The properties of the various railroads are being operated with reasonable efficiency, although not with all the esprit de corps of private management. But the public interest in any event is being fully protected as to service.

Where the public interest is *not* being protected is in the attempted consummation of reorganization plans which wipe out, unnecessarily and unjustly, wide segments of capital, and disrupt others. The result is that a great deal of potential capital which might be devoted to public use in our railroad systems is being scared away. This is one of the great hidden sacrifices inherent in these plans, and one of the compelling reasons in the public interest why these plans should be arrested. Delay of this kind is constructive, desirable and will promote the public welfare.

It is a matter of common knowledge, demonstrated by the evidence produced at the hearings before Committees of both Houses, that the principal railroads affected by these bills are doing as well in many respects, and better in some, than a great many other railroads. The obvious injustice and inequity of rushing the innocent security-holders of these railroads "to the guillotine", so to speak, before Congress has an opportunity (in a few months) of passing on measures to review and correct the policies under which those holders were "condemned" by Governmental fiat, will surely be recognized.

The enactment of this legislation will not cast aside the work done thus far in those reorganizations, but rather will enable a fair and equitable capital structure to be built upon the foundation of the records already made in those proceedings, supplemented by unassailable proof of the subsequent vast improvement in the financial affairs and demonstrated earning power of those carriers.

Appendix A

It is most earnestly hoped by the sponsors of this legislation in both Houses of Congress that the courts of the United States and the Interstate Commerce Commission will take no further steps toward the effectuation or consummation of pending plans or reorganization that may place such plans beyond the reach of Congressional remedy, but will instead cooperate with the Congress and the President in retaining custody of such properties until this pending legislation can be considered and voted on shortly after Congress reconvenes.

CLYDE M. REED,
FRANCIS J. MYERS,
SAM HOBBS,
CHAUNCEY W. REED.

Washington, D. C.
August 1, 1947

Appendix B

IN THE

UNITED STATES CIRCUIT COURT OF APPEALS,

FOR THE EIGHTH CIRCUIT.

Nos. 13367, 13368, 13369, 13371, 13372, 13373—Civil

IN THE MATTER OF MISSOURI PACIFIC RAILROAD COMPANY, DEBTOR

EDMUND WRIGHT, ETC., ET AL.

v.

GROUP OF INSTITUTIONAL INVESTORS, ETC., ET AL. (CONSOLIDATED APPEALS)

MEMORANDUM BRIEF FOR INTERSTATE COMMERCE COMMISSION

This memorandum brief is in response to this Court's request, incorporated in its order of May 24, 1947, that the Interstate Commerce Commission, if so advised, file brief stating its views respecting the issues raised by the appeals.

The Commission has given consideration to the briefs filed by appellants in the light of the record. The Commission by recorded action has decided to recommend to the Court that the Reorganization Plan of the Missouri Pacific as certified by the Commission and approved by the District Court be referred back to it for further hear-

ing and consideration and such revision as it may find to be appropriate.

The reasons which have prompted the Commission to this action follow:

The chief issue raised by the appeals is whether the conditions of the bankrupt's property have so changed since the closing of the record before the Commission and the certification of the plan to the District Court as to make it necessary or desirable to have further Commission consideration.

Subsection (d) of Section 77 provides that if the Commission approves a plan it shall thereupon certify the plan to the Court together with a transcript of the proceedings before it and a copy of the report and order approving the plan, thus fulfilling its administrative function. Thereafter all formal proceedings are before the courts: the views of the parties, their interpretation of any new data and their effect upon the reorganization requirements must be submitted to the courts. The Commission has consistently refrained from volunteering its views on new or changed conditions. At such point in the proceedings it has felt that the question whether conditions have so changed as to require resubmission of the plan to the Commission for revision is primarily one for the District Court before which the facts may be presented and the matter argued. If the court upon review of the conditions existing at the time the plan is before it concludes that changed conditions or other circumstances are such that a review and modification of the plan seems necessary or desirable it may refer the plan back to the Commission. That this is the prescribed statutory procedure is shown by subsection (e) which provides that the district judge may "in his discretion and on motion of any party in interest refer the proceedings back to the Com-

mission for further action, in which event he shall transmit to the Commission a copy of any evidence received.'"[1]

In the instant case the Commission's third supplemental report and order of October 9, 1944, finally approved (after petitions for modification had been filed) the plan of reorganization now pending in this Court (R. 783). In that report the Commission discussed the effect upon the plan of a payment by order of the bankruptcy court of 30 percent of the principal amount of St. Louis, Iron Mountain & Southern (River & Gulf Divisions) first mortgage bonds amounting to $10,352,400 of principal of the bonds. While this payment had not been contemplated at the time of the issuance of its report of July 4, 1944, it was a basis urged subsequently for modification of the plan, and considered in the report of October 9, 1944. In that report the Commission stated that such payment and others should be left to the discretion of the court. Although such payment would result in the non-issuance of $10,352,400 of new collateral trust 3½ percent 10-year notes provided for issue under the plan in satisfaction of this part of these bondholders' claims, as well as $12,940,000 of new series C first mortgage bonds which would be pledged as security for the notes, the Commission stated that it had fixed $560,000,000 as a *maximum* permissible capitalization of the reorganized debtor and that it recognized that distribution of cash by order of the District Court within the framework of the plan might result in a somewhat less capitaliza-

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[1] Compare *Chicago & N. W. Ry. Co.* v. *U. S.*, 52 F. Supp. 65, affirmed *per curiam* 320 U. S. 718. There the Commission denied a motion to reopen the reorganization after confirmation of the plan on grounds of changed conditions. An attempt was made to review this order under the Urgent Deficiencies Act, 28 U. S. C. A., sec. 41 (28), 46, 47. In denying jurisdiction the statutory court held that review of Commission orders in bankruptcy proceedings are limited to the district court sitting in bankruptcy.

tion at the time of consummation (R. 787). The Commission considered that the new securities so released by the payment on this claim should not be distributed to other creditors. This cash payment has been directed by the District Court.

However, since the issuance by the Commission of its last report and order the District Court has authorized other cash payments on the principal of certain obligations of the debtor. The present effect upon the reorganization plan as approved by the Commission may be tabulated thus:

	Amount of claim paid	New securities which would be released if obligations purchased or satisfied are canceled
R. F. C. claim.	$23,134,080	$23,134,800 new first mortgage bonds.
Bank debt	5,850,000	5,850,000 new first mortgage bonds.
R. C. C. claim.	2,487,000	2,487,000 new first mortgage bonds.
River & Gulf bonds	[1] 13,803,200	[1] 13,803,200 new first mortgage bonds (approx.) new class.
Secured serial 5½ percent bonds	895,000	756,725 A common stock. 504,417 (approx.) new class B common stock.
Boonville, St. L. & Sou. bonds	210,500	57,580 (approx.) new first mortgage bonds. 57,580 (approx.) new preferred stock.
	46,380,500	$46,651,302

Under the District Court's orders the bonds acquired through the satisfaction of the River & Gulf mortgage have been cancelled. In all other instances the obligations

[1] Amount shown does not include interest on the bonds. Interest has been paid currently on these bonds.

purchased are held by the trustees of the debtors for the benefit of the holders of Missouri Pacific first and refunding bonds and for the benefit of any other creditors of the debtor to the extent of their respective interests, if any, in the cash used in the purchase of the obligations as the same may appear or may hereafter be determined by the Court or any Reorganization Plan, with right of subrogation (R. 1179). The Court reserved the right to order the obligations purchased to be cancelled should it find such to be in the best interest of the trust estate.

In addition to the above payments of principal and interest on claims, the District Court has, from time to time, ordered payments in large amounts of accrued delinquent interest on the most senior bond issues of the three principal debtors. The plan, however, makes specific provision for these payments. They alone present no reason for further consideration of the plan by the Commission.

Extensive expenditures have been made for improvement of the property. The effect of those upon the earning power of the company may be controversial. Operation of the properties in recent years has resulted in large accumulations of cash in the treasuries of the companies. Some of this cash may be available for distribution to the security holders. While the plan is sufficiently elastic to permit of adjustment for a reasonable amount of debt retirement and interest payment, it is questionable whether the possibility of the large retirements and expenditures and further cash accumulations which have occurred were contemplated. Whether the provisions of the plan should be interpreted as permitting the acquisition of claims for the benefit of other classes of creditors may be doubted.

Adjustment of the plan to meet present conditions involves several major problems. The first is: Should the

securities released through retirement and acquisition of claims be redistributed to other creditors or cancelled? Since the plan may not have contemplated such large retirements, the total permissible capitalization as found by the Commission may be affected.[3] This situation is aggravated by the possibility of further cash distributions.

If it be decided that the released securities should be distributed to the remaining security holders there is involved the determining of their rights in and to the cash used for retiring and acquiring other claims. The exchange of securities and the apportionment of cash under the plan are in accordance with a somewhat involved formula based upon the value of the constituent debtors to the new system, chiefly by reason of their past, present and prospective earnings and, to a certain extent, in the case of a few of the debtors, the strategic importance of their lines of railroad. The formula, however, is not a rigid one, and, in some degree, the allocation of securities and possibly cash, is the result of trading between representatives of the various debtors who participated in the negotiation of the so-called "compromise plan," which, with some changes, was adopted by the Commission. The allocation of cash among the present security holders is in general on the basis of the cash on hand (as of that time) in the treasuries of the three principal debtors.

The working out of a fair and equitable adjustment of the distribution of cash and securities will be a complicated matter. To attempt to do this within the framework of the present plan may result in substantial disturbance of

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[3] The judgment of the Commission on total permissible capitalization is final. *Ecker* v. *Western Pacific R. Corp.*, 318 U. S. 448, 474; *Group of Investors* v. *Milwaukee R. Co.*, 318 U. S 523, 541.

the balanced relationship of the treatment provided for the various classes of creditors.

It is submitted that these problems arising out of the substantial changes in conditions since the approval of the plan justify its further review by the Commission.

There are additional reasons which make it desirable that the Commission give further consideration to the plan. Opportunity will be afforded for reviewing the so-called "cash-option" provisions and determining whether they are practicable under present conditions of the security market. Under the present plan it is necessary for the reorganization managers to purchase new general mortgage bonds and new common stock at certain maximum prices. In this connection there is some question whether both the new class A and class B common stock may be so purchased and as to whether purchases of the new general mortgage bonds and common stock must under the provisions of the plan be made by the reorganization managers immediately at the time of the consummation of the plan or whether they may be purchased as market conditions may permit over a considerable period after consummation of the plan. The terms of the approved plan are not explicit upon these questions.

Again, if the plan be returned to the Commission opportunity will be had of reviewing its provisions as to the selection of the reorganization managers and the first board of directors of the new company. The holdings of present securities of some of the parties entitled under the plan to nominate appointees probably have materially decreased from their original holdings, notably in the case of the Institutional Group of Holders of Missouri Pacific First and Refunding Bonds. In the case of the Reconstruc-

tion Finance Corporation, whose loan has been satisfied, there will be an initial failure of appointment.

For these reasons the Commission is of the opinion that the present plan should be returned to it for reconsideration and revision, and it so recommends.

Respectfully submitted.

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